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Proposed Procedural Changes in Federal Tax Practice

BY J. S. SEIDMAN

IF THE advance blessings pronounced by Secretaries Morgenthau and Hopkins on changes in the tax law that may prove a boon to business extend also to procedural matters, then there are many applicants for the benediction. All has not been quiet on the tax puddles of the Potomac for some time. The serenity of the scene has spasmodically been ruffled by splashes from new procedural courses. Decentralization has been a recent contributor and its tide has not yet reached the high-water mark. That, however, is primarily an intradepartmental cascade and affects *modus operandi* while a case is still being administratively nurtured. More than seasonal torrents have recently poured forth from the Congressional reservoir, dealing with the channeling of the tax case when it leaves the Treasury Department and heads upstream to reach its ultimate judicial source.

Proposals for changes in tax procedure will, like men and the river Avon, come, go, and flow on forever. That is as it should be. However, as we are experiencing right now a ground swell of interest in the subject, in the high and low places, with the consequent probability that sooner or later there will be some actual doings, it is fitting that we pause to note and appraise the views that currently seem to hold sway or have been shouted the loudest from the housetops.

While no single statement or document confines these broad vistas of thought, an excellent panorama is provided by a close study of two recent expressions. One is H.R. 234, introduced by Congressman Celler. The other is an article by Roger John Traynor of the University of California, in the December, 1938, issue of the *Columbia Law Review*. Congressman Celler's bill deals with appellate review of the action of the Treasury Department. Mr. Traynor's article places much emphasis on procedure while a case is under Department surveillance. Through a later bill, Congressman Celler clipped the wings of H.R. 234 in several respects, but as H.R. 234 is of more generic character, it provides the better ingredients for our test tube. Mr. Traynor's views have special interest since he has served as a Treasury consultant. Accordingly, we discuss H.R. 234 and Mr. Traynor's article in turn.

H.R. 234

H.R. 234 covers a vast area and overruns into fields utterly foreign to taxes. However, for our purposes, attention will be confined to tax matters. The bill proposes to set up an administrative court of both original and appellate jurisdiction. One of the four specialties with which this court would deal is tax matters. This would be done by merging into the court fabric the United States Board of Tax Appeals—lock, stock, and barrel—including (at least at the outset) all of the present personnel, practice, and procedure. The members of the board would become federal judges, with increased compensation and life tenure. All tax cases would pivot around this part of the court. The present jurisdiction of the district courts and the Court of Claims in tax matters would cease. There would be commissioners to take testimony and report their conclusions to the court, presumably in the same manner as is now done in Court of Claims matters.

An appellate mechanism would be

supplied within the court itself, through two divisions, one of which would deal solely with taxes (and extraordinary writs and licenses). Appeals would lie as of right. On appeal, questions both of fact and law would be open to review. The jurisdiction of the various circuit courts of appeal in tax cases would no longer exist. Instead, all tax appeals would be heard by the appellate division of the new court. Upon report by the appellate division, there would be a right to petition for a rehearing on questions of law appearing on the record and the petition would be heard by justices of the appellate division a majority of whom would not have participated in the original appeal. The judgment of the appellate division would be subject to review by the Supreme Court on petition for writ of certiorari, just as is now the case with respect to decisions of the circuit courts of appeals.

While there are many other features about the bill, the foregoing outlines the essential framework as it pertains to tax cases. Analysis can perhaps most effectively be undertaken by treating in their separate categories the trial aspects and then the appellate phases. As for the former, what the bill essentially proposes, is to concentrate all tax controversy in the Board of Tax Appeals (in its retitled status as the tax section of the administrative court). The board well merits the confidence and added responsibility which would be thus reposed in it. Frequent have been the proposals at Congressional hearings that its jurisdiction be expanded so that it may decide not only asserted deficiencies, but also claimed refunds. To the extent that the bill would accomplish that objective, it warrants commendation. Laudable, too, is the official recognition of the members as "justices," as well as their increased compensation and life tenure. Then again, if the Court of Claims experience is symptomatic, the use of commissioners to take testimony and report on the facts might inject an informality and a time and geographical convenience that would be relished by taxpayers, the Government, and practitioners.

The bill also presents attractive prospects in other and broader aspects. Today, appeals having to do with deficiencies go to the Board of Tax Appeals. The same taxpayer has to take the same point either to the district court or Court of Claims if a refund is involved for another year. That is an unsatisfactory dispersion. The bill would not only put an end to such vagaries, but also concentrate all tax appeals before a group of specialists. By doing so, it would automatically extirpate that anachronism which makes a procedural fetish out of cases against the collector as distinguished from cases against the United States or the commissioner. Furthermore, it offers a welcome relief from overburden to the various district courts in the termination of their jurisdiction over tax litigation.

So much for matters appertaining to the original jurisdiction of the tax section of the court. As regards the appellate aspects, the concentration of tax appeals before one judicial forum has many advantages. At the present time we have the rather anomalous situation where, from the Board of Tax Appeals as a trial agency, review may be had by any one of ten different bodies. This immediately creates opportunity for diversity and conflict that can be remedied only by further litigation. More painfully, it has brought about situations where decisions of one appellate court (even where certiorari has been denied) have been ignored by both the taxpayer and Government, in the thought, effort, and hope of having a similar point brought before an appellate court in another circuit that might decide the matter differently. Conflict has been sought after as a goal instead of being routed as a disease.

Through one appellate court, conflict as such could not exist. This should im-

part more respect for the decision of the appellate court. It should mollify the administrative difficulties just mentioned. It should also put an end to the added amount of litigation that now inheres in the multitudinous channels of appeal. Besides, the natural and logical order calls for fewer officers than soldiers and fewer appellate courts than trial courts. In appeals from board cases, there is now a numerical inversion. The bill would restore balance.

The ability to have the appellate court review the facts as well as the law, would come nearer to the layman's understanding and appreciation of a real appeal. Also, the rehearing that could be obtained within the court would in a sense substitute for the further review that might otherwise be sought through the Supreme Court. It would certainly assuage the anguish and difficulty now attendant upon getting a case to the Supreme Court. On the other hand, there is an objection from a geographical standpoint to one appellate court. But that objection, if insurmountable, may have to give way, on net balance, to the greater inherent advantages.

The bill has been criticized as being a Goliath and miscegenation of administrative and judicial functions. That is probably aimed at the jurisdiction of the court in matters other than taxation, and hence takes us beyond the province of our interest. Fears have also been expressed that if the general court structure is of Frankenstein proportions, the Board of Tax Appeals will lose its present flavor and be submerged in the shuffle. There is nothing to make it work out that way. To the contrary, the likelihood is that each of the specialized groups within the court would preserve its identity by very reason of the specialization that is involved. If the prospect is otherwise, the bill justifies vigorous opposition from tax practitioners.

Another and even more poignant fear is the possible effect of the bill on the continued right of accountants to present cases in the trial division. The board, in its years of experience, has recognized the accounting profession and legal profession as members of its bar in coördinate standing. It is provided in the bill that the rules of the board shall become the rules of the court, but the very use of the word "court" has a frightening connotation to the accountant who would practise before it. The board has officially been styled not as a court, but as an executive or administrative body, possessing quasi-judicial functions. Accountants are *persona grata* in such a forum. But before a "court" they might be gradually and gently eased out, if not summarily ejected.

Accountants can hardly call for an affirmative provision in the bill, to preserve and perpetuate their present status in trial work, because that status is not vouchsafed by any statutory provision today. But the objective, however to be accomplished, is something to which accountants will undoubtedly feel justified in adhering.

It may be that a solution will develop from the following restatement and clarification of the views here expressed regarding the bill generally: The bill has been considered purely as it touches upon tax cases. In that regard, its proposals on the whole merit commendation. However, all of these favorable features in tax cases can be equally derived from a bill that will be confined solely to taxation and will call for (1) the continuation of the present Board of Tax Appeals, with the amplified jurisdiction now recited in the bill, and (2) the creation of a single court of tax appeals that will function in the manner provided in the bill for the appellate division. Such a measure would cleave tax matters from the others with which they should not be mated. It would give full force to the spirit of specialization and would serve as a reassurance to that

part of the profession of tax practitioners made up of accountants.

It is interesting to note that Mr. Celler supplanted H.R. 234 with a bill dealing solely with a court of appeals. Its logical counterpart will undoubtedly some day find itself reflected in a reorientation of tax practice to embrace the present Board of Tax Appeals as well. Such a step is advanced beyond the speculative stage in Mr. Traynor's recommendations, now to be considered.

Mr. Traynor's Views

Mr. Traynor sees a number of flaws in the present procedure before the Treasury Department: piecemeal presentation of facts, series of innocuous protests, conferences that are devoid of authoritativeness, vague deficiency letters, inconclusive scope of controversy. He also deplores the disparity in procedure where deficiencies are involved as compared with the course of things when refunds are at stake.

If Mr. Traynor had his way, bureau procedure would be adjusted to click in somewhat the following fashion: After report by the revenue agent, informal conference would be available. If the conference resulted in a difference between the parties, a deficiency letter would be sent the taxpayer, affording him an opportunity to present a protest within a time fixed by the commissioner, according to the complexity of the case. If no protest were filed, assessment would follow and that would close the case once and for all against later refunds or additional assessments. (It would presumably work in about the same way as if a closing agreement had been entered into under present-day procedure.) If a protest were filed, it would be a do-or-die affair, and *the taxpayer would thereafter be bound by the issues and facts contained in it.* The protest would have to contain *all* the facts, both ultimate and evidentiary, on which the taxpayer relies and also contain reference to all supporting documents and the names of the people who could support the factual statements made.

Conference on the protest would be held in the field. If, after conference, the parties were still apart, the bureau would send the taxpayer its findings of fact and issues of law (reminiscent, perhaps, of the memorandum the commissioner used to get out on the transmittal of a case to the committee on appeals and review). Appeal to the board would be from these findings. Both sides would be confined to the facts and issues framed through the protest and the findings. No new thrusts by the Government or defenses or claims by the taxpayer could be made. Refunds would go the way of deficiencies. The refund claim would serve as the taxpayer's protest, with the same requirements and consequences. Appeal from the commissioner's findings of fact and issues of law on disallowed refunds would likewise go to the board (thus tieing right in with H.R. 234).

On behalf of such procedure, Mr. Traynor points out several advantages. For one, it would bring about early disclosure of all the facts. This, in turn, would enable both sides the quicker and the better to appraise the strength of their respective positions and reach a settlement, or at least reduce their controversy to one of ultimate facts and law. The conference on the revenue agent's report and the one following the protest, would attain enhanced importance and authority, the one to ward off the need for formal, complete, and binding protest, the other as the last effort to stave off litigation. The commissioner's findings would definitely crystallize the factual and legal story, in substitution of the present deficiency letter that at times is void of any explanatory background.

Mr. Traynor has studied the whole problem with extraordinary insight. He has put his finger on a number of sore spots. He has contributed thought-provoking corrective suggestions. He

recognizes and anticipates some objections. The significance of the protest makes its preparation akin to preparation for trial before the board. That means time, formality, and professional assistance. Mr. Traynor feels that all of these are warranted to insure forthright disposition of a tax controversy. He also foresees possibilities of considerable bickering before the board over the admissibility of evidence, particularly in the determination of whether the line of questioning comes within the ambit of the facts in the protest. The solution of this problem, he says, would be right up to the board and the manner and spirit in which it applied the governing philosophy. Another technical problem would arise if, while a case was pending before the board, new rulings or decisions gave relevancy to certain facts not regarded as pertinent before the protest was filed or the commissioner's findings made. Here the palliative is for the board to step in and, in the guiding light of its discretion, open the doors or keep them shut. Though the point is not covered in the article, presumably the same procedure would apply (in relaxation of the rule that bound the taxpayer to the protest) if the commissioner's findings gave rise to new issues or phases that could not therefore be covered by the protest.

Besides the phases thus called to attention by Mr. Traynor himself, there may be additional items meriting consideration. The core of the proposal is that part of the formal procedure now implicit in board hearings be moved one step down and made the last stage of negotiation in the commissioner's office. Anything that accelerates or augments formality dampens the enthusiasm with which it might otherwise be received. Formality breeds rigidity, irritation, and increased cost. The experience of both the bureau and the taxpayer will undoubtedly attest to the virtues of informality in the administrative stages. There can be no objection to any procedure that results in having the parties get down to cases more quickly and seriously. Formality, however, slows up procedure and is anathema to effective negotiation. Mr. Traynor himself points out that seventy per cent of the dockets closed before the board in the past few years were closed as a result of informal settlements. Yet in all those cases it would have been necessary, under the recommended procedure, that the parties go through the ordeal, spend the time and energy, and bear the cost of preparing for trial in fullest detail through the formal protest and findings that would perforce be involved. It may also be questioned whether the parties would have "gotten together" in all the seventy per cent of the cases once they had both reached the stubborn and pugnacious "record" stage of their controversy.

Mr. Traynor feels that one of the major deterrents to conclusive early negotiation is that the bureau does not have all the facts, and doesn't get them except by gradual extraction from or presentation by the taxpayer—a process frequently not complete until the case has been tried before the board or in court. It may be true that in some cases the revenue agent is not in a position, during the course of his investigation, to obtain all the data needed. Those instances are but occasional. On the whole, the field examination imparts to the bureau all that it seeks. In truth, it is not infrequent that the commissioner is armed with more information than the taxpayer has, since the revenue agent has access to sources not available to the taxpayer.

While full knowledge by both sides of the underlying facts is an essential, if the parties are to be able to compose their differences in forthright fashion, may it not be that in the last analysis, from the bureau's standpoint, it is really a matter of personnel? Given a corps of capable, courageous men, vested with authority and ready to act

upon that authority, procedural problems as such pale in significance and are well-nigh automatically dissipated. Present-day procedure, especially with decentralization, bids fair to advance the administration further toward the attainment of this ideal. It would be a pity to "rock the boat" at this stage with the interpolation of strait-jacketing formalities of the type exemplified by the proposed protest and findings.

The insurmountable confines of the protest and findings are not likely to promote good feeling between the parties. It is somehow repellent to one's innate sense of justice to find that an adequate defense to a tax action cannot be advanced merely because it had not theretofore been presented or couched in proper phraseology in some required document. The legalism may be sound, but taxpayers are not altogether patient with attenuated subtleties. The same holds true on the part of the administrative officials when the Government is on the "short end." Since successful administration has long been recognized to hinge largely on the cooperation of taxpayer and Government, it is well to avoid, if possible, any source of disagreeable infection.

Take another phase. Today many taxpayers, when faced with an additional assessment, prefer to pay on items that are controversial and await the outcome of some test case while their own is protected by refund claim. That is particularly true where small amounts are involved, or with estates and trusts that want to wind up. Under the recommended procedure, it would be necessary for each of these taxpayers to resist payment and litigate to the limit, since voluntary payment would be irretrievable. Under the proposal, an uncontested additional assessment or a disallowed and unlitigated claim or protest would put an end to any possible future recovery. The inevitable effect of such prescription would be a multiplicity of lawsuits and appeals, a deferment of payments to the Treasury, and a hardship on scores of taxpayers. Even if the bureau or the board would agree to a policy to hold cases in abeyance pending the outcome of controversial matter, such a policy could hardly lend itself to complete practical application.

The article does not indicate whether, once a case went to the board, it would still be permissible for settlement to be reached by the parties. To bar settlement would be a drastic cloture; yet to leave it available would weaken the fibre of antecedent procedure.

Mr. Traynor suggests, as a means of stopping the loss of revenue resulting from the uncollectibility of about eleven per cent of the deficiencies determined by the board, that the taxpayer filing a petition with the board be required to post a bond in the amount of the deficiency. Conditioning an appeal to the board upon the filing of a bond would prove onerous. It would of course aid the Government in assuring collection of the deficiency, but the bond would presumably be based on the amount of the deficiency as asserted by the Commissioner, whereas approximately thirty per cent of that amount is what the board has found to be actually payable. Besides, from the taxpayer's standpoint, posting a bond is almost the same as payment, and yet the very purpose sought to be promoted in creating the board was to provide a quasi-judicial mechanism for the disposition of tax disputes without need for any payment in advance.

These comments would lose their point and intent if they were taken as marring in the slightest the constructiveness of Mr. Traynor's study. Mr. Traynor has blazed the road. It is paved, in parts, with blocks from successful English administrative procedure in tax matters. Mr. Traynor has sufficiently illuminated the path so that we can observe it from all angles, and develop our best course.